

# Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other				Local Government Name		County	
Audit Date		Opinion Date		Date Accountant Report Submitted to State:			

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☐ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ Yes ☐ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☐ Yes ☐ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☐ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☐ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ Yes ☐ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☐ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☐ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☐ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.			
Reports on individual federal financial assistance programs (program audits).			
Single Audit Reports (ASLGU).			

Certified Public Accountant (Firm Name)				
Street Address		City	State	ZIP Code
Accountant Signature <i>Abraham &amp; Gellray, P.C.</i> <i>Alan M. Stone</i>			Date	

**City of Montrose  
Genesee County, Michigan**

**FINANCIAL STATEMENTS**

**June 30, 2004**

City of Montrose  
Genesee County, Michigan  
CITY COUNCIL  
June 30, 2004

Eldon Dunklee	Mayor
Deborah Gross	Mayor Pro-Tem
Frank DeForke	Council Member
Norvill Landes	Council Member
Gene Powell	Council Member
Delana Vroman	Council Member
Ruth Vander Hill	Council Member

City of Montrose

Genesee County, Michigan

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Aaron M. Stevens, CPA  
Eric J. Glashouwer, CPA

Karen A. Roka, CPA  
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Alan D. Panter, CPA  
William I. Tucker IV, CPA  
Kurt M. Lemmen, CPA



ABRAHAM & GAFFNEY, P.C.  
Certified Public Accountants

Member:  
American Institute of  
Certified  
Public Accountants  
and  
Michigan Association of  
Certified Public  
Accountants

INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and  
Members of the City Council  
City of Montrose  
Montrose, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, the discretely presented component unit, and the aggregate remaining fund information of the City of Montrose, Michigan as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of City of Montrose's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, based on our audit the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, the business-type activities, each major fund, the discretely presented component unit, and the aggregate remaining fund information of the City of Montrose, Michigan as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note A, the City has implemented a new financial reporting model, as required by the provisions of Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments, as of July 1, 2003, along with all related statements and interpretations.

The management's discussion and analysis and budgetary comparison information as identified in the table of contents are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The City of Montrose, Michigan, has not presented the budgetary comparison information for the Major Street Fund and the Local Street Fund that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statements.

Our audit was made for the purpose of forming opinions on the financial statements that collectively comprise the City of Montrose's basic financial statements. The accompanying other supplementary information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the basic financial statements. The other supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Abraham & Gaffney, P.C.*

ABRAHAM & GAFFNEY, P.C.  
Certified Public Accountants

October 6, 2004

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

The following is a discussion and analysis of City of Montrose's (the City's) financial performance and position, providing an overview of the activities for the year ended June 30, 2004. This analysis should be read in conjunction with the *Independent Auditors Report* and with the City's financial statements, which follow this section. 2003/2004 represents the first year the City implemented the provisions of the Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, as amended by GASB Statement No. 37 *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments - Omnibus* and Statement No. 38 *Certain Financial Statement Note Disclosures*. Therefore, this discussion and analysis provides few comparisons with the previous year. Future reports will include financial comparisons to the prior as required by GASB.

## **FINANCIAL HIGHLIGHTS**

### **Government-wide:**

- Total net assets at the close of the fiscal year were \$3,922,066 (excluding component units).
- Governmental activities net assets were \$706,893.
- Business-type activity net assets were \$3,215,173.
- Component Unit net assets were \$124,537.

### **Fund Level:**

- At the close of the fiscal year, the City's governmental funds reported a combined ending fund balance of \$254,797.
- The General Fund realized \$8,837 more in revenues than anticipated for the fiscal year. However, General Fund operations also expended \$134,245 more than appropriated.
- Overall, the General Fund balance decreased by \$66,879 to \$149,963 - all undesignated and available for general purposes.

### **Capital and Long-term Debt Activities:**

- The total long-term debt for the primary government was \$828,242 with a net reduction of \$35,889 from the prior year.
- The total additions to the capital asset schedule for the primary government were \$334,414 which included additions to infrastructure, capital outlay related to the M-57 water main, and the capital costs of relocating the depot.

## **OVERVIEW OF THE FINANCIAL STATEMENTS**

This discussion and analysis is intended to serve as an introduction to the City's annual financial report. The annual financial report of the City consists of the following components: 1) *Independent Auditors Report*; 2) *Management's Discussion and Analysis* and 3) the *Basic Financial Statements* (government-wide financial statements, fund financial statements, notes to the financial statements), *Required Supplementary Information* such as budget to actual comparisons for the General Fund and major Special Revenue Funds, and *Other Supplementary Information* including combining financial statements for all non-major governmental funds and other funds and financial data.

## City of Montrose Management's Discussion and Analysis

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### **Government-wide Financial Statements (Reporting the City as a Whole)**

The set of government-wide financial statements are made up of the Statement of Net Assets and the Statement of Activities, which report information about the City as a whole, and about its activities. Their purpose is to assist in answering the question, is the City, in its entirety, better or worse off as a result of this fiscal year's activities? These statements, which include all non-fiduciary assets and liabilities, are reported on the *accrual basis of accounting*, similar to a private business. This means revenues are accounted for when they are *earned* and expenses are accounted for when *incurred*, regardless of when the actual cash is received or disbursed.

The Statement of Net Assets (page 1) presents all of the City's assets and liabilities, recording the difference between the two as "net assets". Over time, increases or decreases in net assets measure whether the City's financial position is improving or deteriorating.

The Statement of Activities (page 2) presents information showing how the City's net assets changed during 2003/2004. All changes in net assets are reported based on the period for which the underlying events giving rise to the change occurs, regardless of the timing of related cash flows. Therefore, revenue and expenses are reported in these statements for some items that will only result in cash flows in future financial periods, such as uncollected taxes and earned but unused employee annual leave.

Both statements report the following activities:

- ***Governmental Activities*** - Most of the City's basic services are reported under this category. Taxes, charges for services and intergovernmental revenue primarily fund these services. Most of the City's general government departments, law enforcement, economic development, city improvements, recreation activities, and other City wide elected official operations are reported under these activities.
- ***Business-type Activities*** - These activities operate like private businesses. The City charges fees to recover the cost of the services provided. The Water Fund and the Sewer Fund are examples of these activities.
- ***Discretely Presented Component Units*** - Discretely Presented Component units are legally separate organizations for which the City Council and Administration appoints a majority of the organization's policy board and there is a degree of financial accountability to the City. One organization is included as a discretely presented component unit: the Downtown Development Authority.

As stated previously, the government-wide statements report on an *accrual* basis of accounting. However, the governmental funds report on a *modified accrual* basis. Under modified accrual accounting, revenues are recognized when they are measurable and available to pay obligations of the fiscal period, expenditures are recognized when they are due to be paid from available resources.

Because of the different basis of accounting between the fund statements (described below) and the government-wide statements, pages 4 and 7 present reconciliations between the two statement types. The following summarizes the impact of transitioning from modified accrual to full accrual accounting:

- Capital assets used in governmental activities (depreciation) are not reported on the fund financial statements of the governmental fund. Capital assets and depreciation expense are reported on the government-wide statements.
- Capital outlay spending results in capital assets on the government-wide statements, but is reported as expenditures on the fund financial statements of the governmental funds.



## City of Montrose

### Management's Discussion and Analysis

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- Long-term liabilities, such as amounts accrued for sick and annual leave (compensated absences), etc. appear as liabilities on the government-wide statements; however they will not appear on the fund financial statements unless current resources are used to pay a specific obligation.

#### **Fund Financial Statements (Reporting the City's Major Funds)**

The fund financial statements, which begin on page 3, provide information on the City's significant (major) funds, and aggregated non-major funds. A fund is a fiscal and accounting entity with a self-balancing set of accounts that the City uses to keep track of specific sources of funding and spending for a particular purpose. Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar.

The *basic financial statements* report major funds as defined by the Government Accounting Standards Board (GASB) in separate columns. Statement 34 defines a "major fund" as the General Fund, and any governmental or enterprise fund which has either total assets, total liabilities, total revenues or total expenditures/expenses that equal at least ten (10) percent of those categories for either the governmental funds or the enterprise funds *and* where the individual fund total also exceeds five (5) percent of those categories for governmental and enterprise funds combined. The major funds for City of Montrose include the General Fund, the Major Street Fund, the Local Street Fund, the Sewer Fund, and the Water Fund. All other funds are classified as non-major funds and are reported in aggregate by the applicable fund type. The City includes detailed information on its non-major funds in the other supplementary information section of this report.

The City's funds are divided into three categories - governmental, proprietary, and fiduciary - and use different accounting approaches:

- ***Governmental Funds*** - Most of the City's basic services are reported in the governmental funds. The focus of these funds is how cash and other financial assets that can be readily converted to cash, flow in and out during the course of the fiscal year and how the balances left at year-end are available for spending on future services. Consequently, the governmental fund financial statements provide a detailed *short-term* view that helps determine whether there are more or fewer financial resources that may be expended in the near future to finance the City's programs. Governmental funds include the *General Fund*, as well as *Special Revenue Funds* (use of fund balance is restricted), and *Debt Service Funds* (accounts for resources used to pay long-term debt principal and interest).
- ***Proprietary Funds*** - Services for which the City charges customers (whether outside the City structure or a City department) a fee are generally reported in proprietary funds. Proprietary funds use the same *accrual* basis of accounting used in the government-wide statements and by private business. *Enterprise funds* report activities that provide supplies and/or services to the general public. The City maintains proprietary funds for the sewer system and water system operations.
- ***Fiduciary Funds*** - The City acts as a trustee or fiduciary in certain instances. The City's fiduciary activities are reported in the separate Statement of Net Assets on page 12. These funds, which include trust and agency funds, are reported using the accrual basis of accounting. The government-wide statements *exclude* the fiduciary fund activities and balances because these assets are not available to the City to fund its operations.

## City of Montrose

### Management's Discussion and Analysis

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#### Notes to the Financial Statements

The Notes to the Financial Statements provide additional information that is essential to a full understanding of the detail provided in the government-wide and fund financial statements. The Notes can be found beginning on page 13 of this report.

#### Required Supplementary Information

Following the Basic Financial Statements is additional Required Supplementary Information (RSI), which further explains and supports the information in the financial statements. RSI includes a budgetary comparison schedules for the General Fund and the major special revenue funds.

#### Other Supplementary Information

Other Supplementary Information includes combining financial statements for nonmajor governmental funds and fund financial statements for the component unit. The nonmajor governmental funds are added together, by fund type, and are presented in aggregate single columns in the appropriate basic financial statements.

### FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

As previously stated, City of Montrose's combined net assets were \$3,922,066 at the end of this fiscal year's operations. The net assets of the governmental activities were \$706,893; the business type activities were \$3,215,173.

#### Net Assets as of June 30, 2004

	<b><u>Governmental Activities</u></b>	<b><u>Business- Type Activities</u></b>	<b><u>Total Primary Government</u></b>
Current Assets	\$ 485,297	\$ 2,047,640	\$ 2,532,937
Noncurrent Assets	<u>293,431</u>	<u>2,051,285</u>	<u>2,344,716</u>
<b>Total Assets</b>	<b><u>\$ 778,728</u></b>	<b><u>\$ 4,098,925</u></b>	<b><u>\$ 4,877,653</u></b>
Current Liabilities	\$ 70,300	\$ 93,332	\$ 163,632
Noncurrent Liabilities	<u>1,535</u>	<u>790,420</u>	<u>791,955</u>
<b>Total Liabilities</b>	<b><u>\$ 71,835</u></b>	<b><u>\$ 883,752</u></b>	<b><u>\$ 955,587</u></b>
Net Assets			
Invested in Capital Assets (Net of related debt)	\$ 293,431	\$ 1,179,295	\$ 1,472,726
Restricted	150,501	45,028	195,529
Unrestricted	<u>262,961</u>	<u>1,990,850</u>	<u>2,253,811</u>
<b>Total Net Assets</b>	<b><u>\$ 706,893</u></b>	<b><u>\$ 3,215,173</u></b>	<b><u>\$ 3,922,066</u></b>

**City of Montrose**  
**Management's Discussion and Analysis**

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The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the City's primary government net assets changed during the fiscal year:

**Changes in Net Assets for the Fiscal Year Ending June 30, 2004**

	<b><u>Governmental Activities</u></b>	<b><u>Business Type Activities</u></b>	<b><u>Total</u></b>
<b>Revenues</b>			
Program Revenues			
Charges for Services	\$ 240,180	\$ 641,298	\$ 881,478
Grants and Contributions	143,247	813	144,060
General Revenues			
Property Taxes	369,871	-	369,871
State Shared Revenue	203,769	-	203,769
Investment Earnings	4,378	12,681	17,059
Miscellaneous	<u>3,937</u>	<u>10,059</u>	<u>13,996</u>
<b>Total Revenues</b>	<b>965,382</b>	<b>664,851</b>	<b>1,630,233</b>
<b>Expenses</b>			
General Government	330,511	-	330,511
Public Safety	272,418	-	272,418
Public Works	203,259	-	203,259
Community and Econ. Dev.	4,113	-	4,113
Recreation and Cultural	17,840	-	17,840
Sewer	-	272,473	272,473
Water	<u>-</u>	<u>290,928</u>	<u>290,928</u>
<b>Total Expenses</b>	<b><u>828,141</u></b>	<b><u>563,401</u></b>	<b><u>1,391,542</u></b>
<b>Increase in Net Assets</b>	<b>137,241</b>	<b>101,450</b>	<b>238,691</b>
Net Assets - Beginning	<u>569,652</u>	<u>3,113,722</u>	<u>3,683,374</u>
<b>Net Assets - Ending</b>	<b><u>\$ 706,893</u></b>	<b><u>\$ 3,215,172</u></b>	<b><u>\$ 3,922,065</u></b>

**Governmental Activities:**

The result of 2003/2004 governmental activity was an increase of \$137,241 in net assets to \$706,893. Of the total governmental activities' net assets, \$293,431 is invested in capital assets, \$150,501 is reported as restricted, meaning these assets are legally committed for a specific purpose through statute or by another authority outside the City government. The balance of \$262,961 is listed as unrestricted, having no legal commitment.

## **City of Montrose**

### **Management's Discussion and Analysis**

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#### **Revenues:**

The three largest revenue categories were property taxes at 38% charges for services at 25%, and state shared revenues at 21%. The City levied property tax millage for the year ended June 30, 2004, for general government operations at 16.3525 mills, which is not assigned to any particular activity. Charges for services, which reimburse the City for specific activities, are the second largest source of governmental activity revenue. Examples include rentals, recreation fees, fire protection, and permits. State shared revenue, the third largest source of governmental activity revenue, is also not assigned to any particular activity.

#### **Expenses:**

General government is the largest governmental activity, expending approximately 40% of the governmental activities total and includes the Clerk, Treasurer, and City Manager departments. Public Safety is the second largest area, expending approximately 33% of the governmental activities total on police and fire protection.

#### **Business-type Activities:**

Net assets in business-type activities increased by \$101,450 during 2003/2004. Of the business-type activities' net assets, \$1,179,295 is invested in capital assets less related debt, and \$45,028 is reported as restricted, meaning these assets are legally committed for a specific purpose through statute, or by another authority outside the City government. The balance of \$1,990,850 is listed as unrestricted, having no legal commitment.

### **FINANCIAL ANALYSIS OF THE CITY'S MAJOR AND NON MAJOR FUNDS**

As the City completed 2003/2004, its governmental funds reported *combined* fund balances of \$254,797. This is a net decrease of \$100,322. The net changes are summarized in the following chart:

	<b>General Fund</b>	<b>Major Street</b>	<b>Local Street</b>	<b>Non Major Governmental Funds</b>
<b>Fund Balance 06/30/03</b>	\$ 216,842	\$ 126,239	\$ 11,776	\$ 262
<b>Fund Balance 06/30/04</b>	\$ 149,963	\$ 150,164	\$ ( 66,934 )	\$ 21,604
<b>Net Change</b>	\$ ( 66,879 )	\$ 23,925	\$ ( 78,710 )	\$ 21,342

#### **General Fund:**

The General Fund is the chief operating fund of the City. Unless otherwise required by statute, contractual agreement or Board policy, all City revenues and expenditures are recorded in the General Fund. As of June 30, 2004, the General Fund reported a fund balance of \$149,963. This amount is a decrease of \$66,879 from the fund balance of \$216,842 reported as of June 30, 2003. The 2003/2004 original budget called for a \$58,529 increase of fund balance. The entire fund balance is reported as undesignated.

## **City of Montrose**

### **Management's Discussion and Analysis**

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The General Fund 2003/2004 expenditures exceeded 2003/2004 revenues by \$66,879, however, the General Fund also supported the operations of the Local Street fund during this fiscal year. The Local Street Fund collectively received \$55,619 in support from the General Fund in 2003/2004.

#### **Major Street Fund:**

As of June 30, 2004, the Major Street Fund reported a fund balance of \$150,164, an increase of \$23,925 from the prior year. The total fund balance is undesignated/unreserved.

#### **Local Street Fund:**

As of June 30, 2004, the Local Street Fund reported a fund deficit of \$66,934, which is a decrease of \$78,710 from the prior year. The General Fund and the Major Street Fund transferred \$55,619 and \$20,397, respectively, to the Local Street Fund to help finance a portion of the 2003/2004 capital street projects. The total fund balance is undesignated/unreserved.

#### **Sewer Fund:**

As of June 30, 2004, the Sewer Fund reported total net assets of \$1,940,531, an increase of \$26,483 from the prior year. Of the total net assets, \$815,966 is reported as the amount invested in capital assets, net of related debt.

#### **Water Fund:**

As of June 30, 2004, the Water Fund reported total net assets of \$1,274,641, which is an increase of \$74,967 from the prior year. Of the total net assets, \$363,329 is reported as the amount invested in capital assets, net of related debt and \$45,028 is restricted for debt service.

#### **General Fund Budgetary Highlights:**

The City of Montrose's budget is a dynamic document. Although adopted in June (prior to the start of the year), the budget is routinely amended during the course of the year to reflect changing operational demands.

Actual General Fund revenue totaled \$747,487; \$8,837 above the final amended budget. Actual General Fund revenues for property taxes exceeded budgeted amounts by \$52,966 due to the City settling the taxes for the 1998, 1999, and 2001 levies. This positive variance was offset by the City not receiving \$27,343 of Federal CDBG revenue that they had budgeted to receive. Also the revenue budget fell short on State revenue sharing by \$15,179. This budget shortfall was due to budget cuts at the State level which are trickling down to local municipalities.

Actual City expenditures and other financing uses for 2003/2004 exceeded budgeted amounts by a total of \$134,245. This negative variance is due to several reasons, including:

- \$12,066 more than planned expenditures in the Mayor's Department.
- \$29,925 more than planned expenditures in the Clerk's Department.
- \$25,737 more than planned expenditures in the Treasurer's Department.
- \$35,962 more than planned expenditures in the Police Services Department.

There were no formal budget amendments approved by City Council throughout the year.

**City of Montrose**  
**Management's Discussion and Analysis**

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**CAPITAL ASSETS AND DEBT ADMINISTRATION**

Capital Assets - At the end of Fiscal Year 2003/2004, the City had invested \$2,287,726, and \$131,312 for the component units, net of accumulated depreciation, in a broad range of capital assets (see table below). Accumulated depreciation was \$2,510,886 for the primary government. Depreciation charges for the fiscal year totaled \$112,508 for the primary government and \$4,911 for the component unit. Additional information related to capital assets is detailed in Note F of the Financial Statements. Net Book value of capital assets at June 30, 2004 was as follows:

	<b>Governmental Activities</b>	<b>Business- type Activities</b>	<b>Component Unit DDA</b>	<b>Total</b>
<b>Land</b>	\$ 99,000	\$ 50,620	\$ 38,000	<b>\$ 187,620</b>
<b>Construction in progress</b>	10,000	-	-	<b>10,000</b>
<b>Vehicles and equipment, net</b>	42,583	-	-	<b>42,583</b>
<b>Infrastructure, net</b>	141,848	-	93,312	<b>235,160</b>
<b>Sewer system, net</b>	-	765,346	-	<b>765,346</b>
<b>Water system, net</b>	-	1,178,329	-	<b>1,178,329</b>
<b>Capital assets, net</b>	<b>\$ 293,431</b>	<b>\$1,994,295</b>	<b>\$ 131,312</b>	<b>\$ 2,419,038</b>

Long-term Debt - As of June 30, 2004, the City had \$828,242 in loans outstanding for the primary government. This level of net obligation is \$35,889 less than the obligation recorded as of June 30, 2003.

**Outstanding Debt as of June 30, 2004:**

	<b><u>July 1, 2003</u></b>	<b><u>Additions</u></b>	<b><u>Deletions</u></b>	<b><u>June 30, 2004</u></b>
<b>Primary Government</b>				
Governmental Activities				
Compensated absences	\$ 1,185	\$ 861	\$ -	\$ 2,046
Business-type Activities				
Revenue Bonds	850,000	-	35,000	815,000
Compensated absences	12,946	-	1,750	11,196
<b>Total Primary Government</b>	<b>864,131</b>	<b>861</b>	<b>36,750</b>	<b>828,242</b>
<b>Component Unit</b>				
Note payable	15,978	-	15,978	-
<b>Total Reporting Entity</b>	<b>\$ 880,109</b>	<b>\$ 861</b>	<b>\$ 52,728</b>	<b>\$ 828,242</b>

A more detailed discussion of the City's long-term debt obligations is presented in Note G to the financial statements.

**City of Montrose**  
**Management's Discussion and Analysis**

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**CITY OF MONTROSE GOVERNMENT ECONOMIC OUTLOOK:**

- State revenue sharing has declined nearly \$30,000 over the past three years, and may face additional cuts due to state budget problems.
- Property tax revenue has not kept pace with inflation.
- Investment earnings are at historically low levels due to low market interest rates, decreasing by nearly 80% over the past four years.
- Health and dental insurance premiums are rising much faster than the rate of inflation.
- Utility costs are rising faster than the rate of inflation.
- Hazard/Liability Insurance costs are rising faster than the rate of inflation.

These factors were considered in adopting the Budget for 2004/2005. An addition of \$435 of the City's fund balance was included to balance the General Fund Budget. The City continues to look for ways to increase efficiencies and reduce the cost of doing business.

**CONTACTING THE CITY**

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If there are questions about this report, or a need for additional information, contact the City of Montrose's Office at (810) 639-6168.

## **BASIC FINANCIAL STATEMENTS**



City of Montrose

STATEMENT OF NET ASSETS

June 30, 2004

	Primary Government			Component Units
	Governmental Activities	Business-type Activities	Total	
ASSETS				
Current assets				
Cash and cash equivalents	\$ 350,006	\$ 1,807,010	\$ 2,157,016	\$ 33,366
Receivables	160,786	94,744	255,530	-
Due from other governmental units	44,906	-	44,906	11,180
Internal balances	(116,959)	145,885	28,926	(28,926)
Due from fiduciary fund	46,558	-	46,558	-
Total current assets	485,297	2,047,639	2,532,936	15,620
Noncurrent assets				
Cash and cash equivalents - restricted	-	56,990	56,990	-
Capital assets, net	293,431	1,994,295	2,287,726	131,312
Total noncurrent assets	293,431	2,051,285	2,344,716	131,312
TOTAL ASSETS	778,728	4,098,924	4,877,652	146,932
LIABILITIES				
Current liabilities				
Accounts payable	61,562	44,192	105,754	-
Accrued liabilities	6,982	1,402	8,384	-
Accrued interest payable	-	9,938	9,938	-
Due to other governmental units	1,245	-	1,245	22,395
Current portion of compensated absences	511	2,800	3,311	-
Current portion of long-term debt	-	35,000	35,000	-
Total current liabilities	70,300	93,332	163,632	22,395
Noncurrent liabilities				
Compensated absences	1,535	8,396	9,931	-
Customer deposits	-	2,024	2,024	-
Noncurrent portion of long-term debt	-	780,000	780,000	-
Total noncurrent liabilities	1,535	790,420	791,955	-0-
TOTAL LIABILITIES	71,835	883,752	955,587	22,395
NET ASSETS				
Invested in capital assets, net of related debt	293,431	1,179,295	1,472,726	131,312
Restricted for:				
Debt service	337	45,028	45,365	-
Streets	150,164	-	150,164	-
Unrestricted	262,961	1,990,849	2,253,810	(6,775)
TOTAL NET ASSETS	\$ 706,893	\$ 3,215,172	\$ 3,922,065	\$ 124,537

See accompanying notes to financial statements.

City of Montrose

STATEMENT OF ACTIVITIES

Year Ended June 30, 2004

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets			
		Charges for Services	Operating Grants and Contributions	Primary Government			Component Units
				Governmental Activities	Business-type Activities	Total	
Primary government:							
Governmental activities:							
General government	\$ 330,511	\$ 12,550	\$ -	\$ (317,961)	\$ -	\$ (317,961)	\$ -
Public safety	272,418	82,218	-	(190,200)	-	(190,200)	-
Public works	203,259	145,412	121,947	64,100	-	64,100	-
Community and economic development	4,113	-	21,300	17,187	-	17,187	-
Recreation and cultural	17,840	-	-	(17,840)	-	(17,840)	-
Total governmental activities	828,141	240,180	143,247	(444,714)	-0-	(444,714)	-0-
Business-type activities:							
Sewer	272,473	292,262	-	-	19,789	19,789	-
Water	290,928	349,036	813	-	58,921	58,921	-
Total business-type activities	563,401	641,298	813	-0-	78,710	78,710	-0-
Total primary government	<u>\$ 1,391,542</u>	<u>\$ 881,478</u>	<u>\$ 144,060</u>	(444,714)	78,710	(366,004)	-0-
Component unit:							
Downtown Development Authority	<u>\$ 18,867</u>	<u>\$ -0-</u>	<u>\$ 56,156</u>	-	-	-0-	37,289
		General revenues:					
		Property taxes		369,871	-	369,871	46,846
		State shared revenues		203,769	-	203,769	-
		Investment earnings		4,378	12,681	17,059	701
		Miscellaneous		3,937	10,059	13,996	120
		Total general revenues		581,955	22,740	604,695	47,667
		Change in net assets		137,241	101,450	238,691	84,956
		Net assets, beginning of the year		569,652	3,113,722	3,683,374	39,581
		Net assets, end of the year		<u>\$ 706,893</u>	<u>\$ 3,215,172</u>	<u>\$ 3,922,065</u>	<u>\$ 124,537</u>

See accompanying notes to financial statements.

City of Montrose

GOVERNMENTAL FUNDS BALANCE SHEET

June 30, 2004

	General	Major Street	Local Street	Nonmajor Governmental Funds	Total Governmental Funds
<b>ASSETS</b>					
Cash and cash equivalents	\$ 139,751	\$ 92,227	\$ 89,827	\$ 28,201	\$ 350,006
Receivables					
Accounts	75	-	-	-	75
Special assessment	-	29,941	130,770	-	160,711
Due from other governmental units	25,919	13,852	5,135	-	44,906
Due from other funds	71,824	20,844	75,740	-	168,408
Due from component unit	28,926	-	-	-	28,926
Advance to other funds	-	91,095	-	-	91,095
<b>TOTAL ASSETS</b>	<b>\$ 266,495</b>	<b>\$ 247,959</b>	<b>\$ 301,472</b>	<b>\$ 28,201</b>	<b>\$ 844,127</b>
<b>LIABILITIES AND FUND BALANCES (DEFICIT)</b>					
<b>LIABILITIES</b>					
Payables					
Accounts	\$ 11,279	\$ 974	\$ 49,309	\$ -	\$ 61,562
Accrued wages	5,642	173	1,167	-	6,982
Due to other governmental units	-	1,245	-	-	1,245
Due to other funds	99,611	65,462	96,065	6,597	267,735
Deferred revenue	-	29,941	130,770	-	160,711
Advance from other funds	-	-	91,095	-	91,095
<b>TOTAL LIABILITIES</b>	<b>116,532</b>	<b>97,795</b>	<b>368,406</b>	<b>6,597</b>	<b>589,330</b>
<b>FUND BALANCES (DEFICIT)</b>					
Unreserved					
Undesignated, reported in:					
General fund	261,201	-	-	-	261,201
Special revenue funds	-	150,164	(66,934)	21,267	104,497
Debt service fund	-	-	-	337	337
<b>TOTAL FUND BALANCES (DEFICIT)</b>	<b>261,201</b>	<b>150,164</b>	<b>(66,934)</b>	<b>21,604</b>	<b>366,035</b>
<b>TOTAL LIABILITIES AND FUND BALANCES (DEFICIT)</b>	<b>\$ 377,733</b>	<b>\$ 247,959</b>	<b>\$ 301,472</b>	<b>\$ 28,201</b>	<b>\$ 955,365</b>

See accompanying notes to financial statements.

City of Montrose

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET  
TO THE STATEMENT OF NET ASSETS

June 30, 2004

**Total fund balance - governmental funds** \$ 366,035

Amounts reported for the governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources  
and therefore are not reported as assets in the governmental funds.

The cost of capital assets is	\$ 489,744
Accumulated depreciation is	<u>(196,313)</u>

Capital assets, net	293,431
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Long-term receivables are not available to pay for current period expenditures  
and are therefore deferred in the funds. These consist of:

Deferred revenue	160,711
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Long-term liabilities are not due and payable in the current period and  
therefore are not reported in the Governmental Funds Balance Sheet.  
Long-term liabilities at year-end consist of:

Compensated absences	<u>(2,046)</u>
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<b>Net assets of governmental activities</b>	<u><u>\$ 818,131</u></u>
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See accompanying notes to financial statements.

## City of Montrose

## Governmental Funds

## STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

Year Ended June 30, 2004

	General	Major Street
REVENUES		
Taxes	\$ 399,974	\$ -
Licenses and permits	31,163	-
Intergovernmental	203,769	91,730
Charges for services	57,228	-
Fines and forfeits	6,377	-
Interest and rents	45,039	1,255
Other	3,937	7,560
TOTAL REVENUES	747,487	100,545
EXPENDITURES		
General government	326,833	-
Public safety	272,418	-
Public works	127,582	56,223
Community and economic development	4,074	-
Recreation and cultural	17,840	-
Capital outlay	10,000	-
TOTAL EXPENDITURES	758,747	56,223
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	(11,260)	44,322
OTHER FINANCING SOURCES (USES)		
Operating transfers in	-	-
Operating transfers out	55,619	(20,397)
TOTAL OTHER FINANCING SOURCES (USES)	55,619	(20,397)
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING USES	44,359	23,925
Fund balances, beginning of year	216,842	126,239
Fund balances (deficit), end of year	\$ 261,201	\$ 150,164

See accompanying notes to financial statements.

Local Street	Nonmajor Governmental Funds	Total Governmental Funds
\$ -	\$ -	\$ 399,974
-	-	31,163
30,217	-	325,716
-	-	57,228
-	-	6,377
457	81	46,832
12,856	21,300	45,653
43,530	21,381	912,943
-	-	326,833
-	-	272,418
198,256	-	382,061
-	39	4,113
-	-	17,840
-	-	10,000
198,256	39	1,013,265
(154,726)	21,342	(100,322)
76,016	-	76,016
-	-	35,222
76,016	-0-	111,238
(78,710)	21,342	10,916
11,776	262	355,119
\$ (66,934)	\$ 21,604	\$ 366,035

City of Montrose

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES,  
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

Year Ended June 30, 2004

**Net change in fund balances - total governmental funds** \$ 10,916

Amounts reported for governmental activities in the statement of activities are different because:

Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:

Capital outlay	\$ 158,444
Depreciation expense	<u>(14,913)</u>

Excess of capital outlay over depreciation expense	143,531
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Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	94,893
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Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:

(Increase) in accrued compensated absences	<u>(861)</u>
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<b>Change in net assets of governmental activities</b>	<u><u>\$ 248,479</u></u>
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See accompanying notes to financial statements.

City of Montrose

Proprietary Funds

STATEMENT OF NET ASSETS

June 30, 2004

	Sewer Fund	Water Fund	Total
<b>ASSETS</b>			
Current assets			
Cash and cash equivalents	\$ 1,046,838	\$ 760,172	\$ 1,807,010
Accounts receivable	44,397	50,347	94,744
Due from other funds	117,919	75,505	193,424
Total current assets	1,209,154	886,024	2,095,178
Noncurrent assets			
Cash - restricted	-	56,990	56,990
Capital assets, net of accumulated depreciation	815,966	1,178,329	1,994,295
Total noncurrent assets	815,966	1,235,319	2,051,285
<b>TOTAL ASSETS</b>	<b>2,025,120</b>	<b>2,121,343</b>	<b>4,146,463</b>
<b>LIABILITIES</b>			
Current liabilities			
Accounts payable	31,132	13,060	44,192
Wages payable	505	897	1,402
Other accrued liabilities	-	9,938	9,938
Due to other funds	47,354	185	47,539
Current portion of compensated absences	1,400	1,400	2,800
Current portion of long-term debt	-	35,000	35,000
Total current liabilities	80,391	60,480	140,871
Noncurrent liabilities			
Payable from restricted cash - customer deposits payable	-	2,024	2,024
Compensated absences	4,198	4,198	8,396
Bonds payable	-	780,000	780,000
Total noncurrent liabilities	4,198	786,222	790,420
<b>TOTAL LIABILITIES</b>	<b>84,589</b>	<b>846,702</b>	<b>931,291</b>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	815,966	363,329	1,179,295
Restricted for debt service	-	45,028	45,028
Unrestricted	1,124,565	866,284	1,990,849
<b>TOTAL NET ASSETS</b>	<b>\$ 1,940,531</b>	<b>\$ 1,274,641</b>	<b>\$ 3,215,172</b>

See accompanying notes to financial statements.



City of Montrose

Proprietary Funds

STATEMENT OF REVENUE, EXPENSES, AND CHANGES IN FUND NET ASSETS

Year Ended June 30, 2004

	Sewer Fund	Water Fund	Total
OPERATING REVENUES			
Charges for services			
User charges	\$ 283,285	\$ 236,479	\$ 519,764
Tap in fees	8,200	22,400	30,600
Other	-	10,059	10,059
TOTAL OPERATING REVENUES	291,485	268,938	560,423
OPERATING EXPENSES			
Salaries and wages	20,059	27,084	47,143
Fringe benefits	21,487	22,377	43,864
Contractual service	146,651	140,007	286,658
Supplies	5,406	5,958	11,364
Utilities	3,506	5,705	9,211
Insurance	2,772	2,772	5,544
Repairs and maintenance	11,951	189	12,140
Equipment rental	1,405	4,429	5,834
Other	919	1,066	1,985
Depreciation	58,317	39,278	97,595
TOTAL OPERATING EXPENSES	272,473	248,865	521,338
OPERATING INCOME	19,012	20,073	39,085
NONOPERATING REVENUES (EXPENSES)			
Intergovernmental	-	813	813
Hydrant assessments	-	13,555	13,555
Special assessments	777	76,602	77,379
Interest revenue	6,694	5,987	12,681
Paying agent fees	-	(1,000)	(1,000)
Interest expense	-	(41,063)	(41,063)
TOTAL NONOPERATING REVENUES (EXPENSES)	7,471	54,894	62,365
CHANGE IN NET ASSETS	26,483	74,967	101,450
Net assets, beginning of year	1,914,048	1,199,674	3,113,722
Net assets, end of year	<u>\$ 1,940,531</u>	<u>\$ 1,274,641</u>	<u>\$ 3,215,172</u>

See accompanying notes to financial statements.

City of Montrose

Proprietary Funds

STATEMENT OF CASH FLOWS

Year Ended June 30, 2004

	Sewer System	Water System	Total
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Cash receipts from customers	\$ 262,783	\$ 297,891	\$ 560,674
Cash paid to suppliers	(200,497)	(216,606)	(417,103)
Cash paid for employee benefits	(21,487)	(22,377)	(43,864)
Cash paid to employees	(20,753)	(28,135)	(48,888)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>20,046</b>	<b>30,773</b>	<b>50,819</b>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>			
Intergovernmental	-	813	813
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>			
Hydrant assessments	-	13,555	13,555
Special assessments	-	76,602	76,602
Paying agent fees	-	(1,000)	(1,000)
Interest expense	-	(41,500)	(41,500)
Capital purchases	-	(175,970)	(175,970)
Payments on borrowings	-	(35,000)	(35,000)
<b>NET CASH (USED) BY CAPITAL AND RELATED FINANCING ACTIVITIES</b>	<b>-0-</b>	<b>(163,313)</b>	<b>(163,313)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Interest revenue	6,694	5,987	12,681
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>26,740</b>	<b>(125,740)</b>	<b>(99,000)</b>
Cash and cash equivalents, beginning of year	1,020,098	942,902	1,963,000
Cash and cash equivalents, end of year	<u>\$ 1,046,838</u>	<u>\$ 817,162</u>	<u>\$ 1,864,000</u>

City of Montrose

Proprietary Funds

STATEMENT OF CASH FLOWS - CONTINUED

Year Ended June 30, 2004

	Sewer System	Water System	Total
Reconciliation of operating income to net cash provided by operating activities			
Operating income	\$ 19,789	\$ 20,073	\$ 39,862
Adjustments to reconcile operating income to net cash provided by operating activities			
Depreciation	58,317	39,278	97,595
(Increase) in accounts receivable	(22)	(1,533)	(1,555)
(Increase) decrease in due from other funds	(29,457)	30,486	1,029
(Decrease) in accounts payable	(32,648)	(36,490)	(69,138)
(Decrease) in wages payable	(694)	(1,051)	(1,745)
Increase (decrease) in due to other funds	4,761	(19,990)	(15,229)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 20,046</u>	<u>\$ 30,773</u>	<u>\$ 50,819</u>

See accompanying notes to financial statements.

City of Montrose

Fiduciary Fund

STATEMENT OF FIDUCIARY NET ASSETS

June 30, 2004

	<u>Current Tax Collection</u>
ASSETS	
Cash	\$ 67,107
Due from other funds	<u>333</u>
TOTAL ASSETS	<u><u>\$ 67,440</u></u>
LIABILITIES	
Due to other funds	\$ 46,891
Due to other governmental units	<u>20,549</u>
TOTAL LIABILITIES	<u><u>\$ 67,440</u></u>

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The City of Montrose is located in Genesee County, Michigan and has a population of approximately 1,811. The City of Montrose operates with a Council form of government and provides services to its residents in many areas including general government, highways and streets, human services, and utilities services.

The City has six (6) City Council members who are elected at large for overlapping four (4) year terms and a Mayor elected at large for a two (2) year term. The Council appoints the Treasurer, Clerk, and Assessor.

The financial statements of the City have been prepared in accordance with generally accepted accounting principles (GAAP) as applied to City governments. The Governmental Accounting Standards Board is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The City's more significant accounting policies are described below.

1. Reporting Entity

As required by accounting principles generally accepted in the United States of America; GASB Statement 14, The Financial Reporting Entity; and Statement on Michigan Governmental Accounting and Auditing No. 5, these financial statements present the financial activities of the City of Montrose (primary government) and its component unit, an entity for which the government is considered to be financially accountable. The discretely presented component unit is reported in a separate column in the government-wide financial statements to emphasize that it is legally separate from the City.

2. Discretely Presented Component Unit

The component unit columns in the financial statements include the financial data of the City's component unit (Downtown Development Authority). The governing body of the Downtown Development Authority is appointed by the City Council, the Authority's budget is subject to the approval of the City Council and the City temporarily relinquishes part of its tax base to the Authority (tax increment revenues).

3. Basis of Presentation

**GOVERNMENT-WIDE FINANCIAL STATEMENTS**

The statement of net assets and the statement of activities (the government-wide statements) present information for the primary government and its component unit as a whole. All non-fiduciary activities of the primary government are included (i.e., fiduciary fund activities are not included in the government-wide statements). For the most part, interfund activity has been eliminated in the preparation of these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities presents the direct functional expenses of the primary government and its component unit and the program revenues that support them. Direct expenses are specifically associated with a service, program, or department and are therefore clearly identifiable to a particular function. Program revenues are associated with specific functions and include charges to recipients of goods or services and grants and contributions that are restricted to meeting the operational or capital requirements of that function. Revenues that are not required to be presented as program revenues are general revenues. This includes all taxes, interest, and unrestricted State revenue sharing payments and other general revenues and shows how governmental functions are either self-financing or supported by general revenues.

**FUND FINANCIAL STATEMENTS**

The fund financial statements present the City's individual major funds and aggregated nonmajor funds. Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

3. Basis of Presentation - continued

FUND FINANCIAL STATEMENTS - CONTINUED

The major funds of the City are:

- a. The General Fund is the City's primary operating fund. It accounts for all financial resources of the general government except for those that are required to be accounted for in another fund.
- b. The Major Street Fund is used to account for the financial resources that are used for repairs and maintenance of the City's major streets.
- c. The Local Street Fund is used to account for the financial resources that are used for repairs and maintenance of the City's local streets
- d. The Sewer Fund accounts for resources generated by providing sewer services to residents of the City, the costs (expenses, including depreciation) are financed or recovered primarily through user charges.
- e. The Water Fund accounts for resources generated by providing water services to residents of the City, the costs (expenses, including depreciation) are financed or recovered primarily through user charges.

4. Measurement Focus

The government-wide and proprietary fund financial statements are presented using the economic resources measurement focus, similar to that used by business enterprises or not-for-profit organizations. Because another measurement focus is used in the governmental fund financial statements, reconciliations to the government-wide statements are provided that explain the differences in detail.

All governmental funds are presented using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

There is no measurement focus for the fiduciary agency fund since assets equal liabilities.

5. Basis of Accounting

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied.

All governmental and similar trust funds are accounted for using the modified accrual basis of accounting. Under this method, revenues are recognized when they become susceptible to accrual (when they become both "measurable" and "available to finance expenditures of the current period"). Revenues that are considered measurable but not available are recorded as a receivable and deferred revenue. Significant revenues susceptible to accrual are special assessments and certain intergovernmental revenues. Expenditures are generally recognized under the modified accrual basis of accounting when the related fund liability is incurred, except for interest on long-term debt which is recorded when due.

All proprietary funds are accounted for using the accrual basis of accounting. Their revenues are recognized when they are earned, and their expenses are recognized when they are incurred.

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

5. Basis of Accounting - continued

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Enterprise Funds are charges to customers for sales and services. Operating expenses for enterprise funds include the costs of sales and services, administrative expenses, and other costs of running the activity. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. If/when both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

6. Budgets and Budgetary Accounting

The General and Special Revenue Funds' budgets are prepared on a basis consistent with the modified accrual basis used to reflect actual results. The City employs the following procedures in establishing its budgetary data.

- a. Prior to April 15, the City Manager submits to the City Council a proposed operating budget for the fiscal year beginning the following July 1. The operating budget includes proposed expenditures and the means of financing them.
- b. A Public Hearing is conducted to obtain taxpayers' comments.
- c. Prior to the second week of May, the budget is legally adopted by appropriating the funds necessary to operate.
- d. The budget is legally adopted at the functional level for the General Fund and Special Revenue Funds.
- e. The City does not employ encumbrance accounting as an extension of formal budgetary integration in the governmental funds. Appropriations unused at June 30 are not carried forward to the following fiscal year.
- f. Any revisions to the budget must be approved by the City Council.

7. Cash and Cash Equivalents

Cash and cash equivalents consist of various savings and money market checking accounts and pooled investment accounts. The cash and cash equivalents are recorded at cost, which approximates market value.

8. Restricted Cash

A portion of the cash and cash equivalents of the Water Fund is classified as restricted cash because its use is limited. The Water Fund's restrictions are due to bond resolution requirements to maintain certain balances in separate accounts for debt service and general purpose reserves, and also for the amount of customer deposits held at June 30, 2004.

9. Property Tax

The City of Montrose bills and collects its own property taxes and also taxes for other governmental units. The City's property tax revenue recognition policy and related tax calendar disclosures are highlighted in the following paragraph.

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

9. Property Tax - continued

Property taxes are levied by the City of Montrose on July 1 and December 1 and are payable without penalty through September 30 and February 28, respectively. The July 1 levy is composed of the City's millage, special assessments, and the school taxes. The December 1 levy is composed of county, school taxes, and special assessments. All real property taxes not paid to the City by March 1 are turned over to the Genesee County Treasurer for collection. The Genesee County Treasurer purchases the receivables of all taxing districts on any delinquent real property taxes. Delinquent personal property taxes are retained by the City for subsequent collection. Collections and remittances of all taxes are accounted for in the Current Tax Collections Agency Fund. City property tax revenues are recognized as revenues in the fiscal year levied.

The City is permitted to levy taxes up to 20 mills (\$20 per \$1,000 of taxable valuation) for general governmental services. For the year ended June 30, 2004, the City levied 16.3525 mills per \$1,000 of assessed valuation for general governmental services. The total Taxable Value for the 2003 levy for property within the City was \$22,702,424.

10. Interfund Transactions

During the course of normal operations, the City has numerous transactions between funds, including expenditures and transfers of resources to provide services, construct assets, and service debt. The accompanying financial statements generally reflect such transactions as operating transfers. Transfers between governmental and proprietary funds are netted as part of the reconciliation to the government-wide financial statements.

11. Compensated Absences

City employees are granted sick and vacation leave in varying amounts. In the event of termination, an employee is paid for accumulated sick and vacation time. All employees with accumulated unused sick and vacation time pay at June 30, 2004 were vested and the total due to them, along with the related payroll taxes, is recorded in the governmental-wide financial statements. For proprietary funds, the cost is recorded as a fund liability when earned.

12. Capital Assets

Capital assets include land, buildings, equipment, and vehicles and are recorded (net of accumulated depreciation, if applicable) in the government-wide financial statements under the governmental activities and component unit columns. Capital assets are those with an initial individual cost of \$1,500 or more and an estimated useful life of more than one year. Capital assets are not recorded in the governmental funds. Instead, capital acquisition and construction are reflected as expenditures in governmental funds, and the related assets are reported in the government-wide financial statements. All purchased capital assets are valued at cost where historical records are available and at an estimated historical cost where no historical records exist. Donated capital assets are valued at their estimated fair market value on the date received.

GASB Statement No. 34 requires major networks and major subsystems of infrastructure assets acquired, donated, constructed, or substantially rehabilitated since fiscal years ending after June 30, 1980, be inventoried and capitalized by the fourth anniversary of the mandated date of adoption of the other provisions of GASB Statement No. 34. The City of Montrose has capitalized the current year's infrastructure, as required by GASB Statement No. 34, and has reported the infrastructure in the Statement of Net Assets. The City of Montrose will retroactively capitalize the major infrastructure assets on or before June 30, 2008, as permitted by GASB Statement No. 34.



NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

12. Capital Assets - continued

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Depreciation is computed using the straight-line method over the following useful lives:

Sewer and Water systems and improvements	10 - 50 years
Equipment and machinery	3 - 12 years
Buildings	25 years
Vehicles	10 years
Infrastructure	20 - 50 years

As a result of the implementation of GASB 34, the City is, for the first time, accounting for infrastructure assets on its financial statements. The government-wide financial statements include those infrastructure assets that were either completed during the current fiscal year or considered construction in progress at current fiscal year-end. However, the government-wide financial statements do not reflect those infrastructure assets completed prior to July 1, 2003. From this point forward, new infrastructure will be added to the records while the retroactive historical value of the City's infrastructure assets will be added prior to June 30, 2008, in accordance with GASB 34.

13. Long-term Liabilities

Long-term debt and other long-term obligations are recognized as a liability in the government-wide financial statements and proprietary fund types when incurred. The portion of those liabilities expected to be paid within the next year is a current liability with the remaining amounts shown as long-term.

Long-term debt is recognized as a liability of a governmental fund when due. For other long-term obligations, only that portion expected to be financed from expendable available financial resources is reported as a fund liability of a governmental fund.

14. Comparative Data

Comparative data for the prior year has not been presented in all funds in the accompanying financial statements since their inclusion would make the financial statements unduly complex and difficult to read.

15. Accounting Change

As of July 1, 2003, the City implemented the provisions of Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments (Statement) along with all related statements and interpretations. Some of the significant changes in the Statement include the following:

- A Management Discussion and Analysis (MD&A) section providing an analysis of the City's overall financial position and results of operations has been included.
- Government-wide financial statements (statement of net assets and statement of activities) prepared using full accrual accounting for all of the City's activities have been provided. Reconciliations are presented between the governmental fund level (modified accrual) and government-wide (full accrual) statements since their measurement focus is not the same.

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE A: DESCRIPTION OF CITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED**

15. Accounting Change - continued

- Long-term obligations reported on the statement of net assets include \$1,185, which was previously reported in the General Long-term Debt Account Group.
- The fund financial statements focus on major funds rather than fund types.

This implementation has also required certain disclosures to be made in the notes to the financial statements concurrent with the implementation of Statement No. 34 based on GASB Statement No. 38. Certain note disclosures have been added and/or amended, including descriptions of activities of major funds and interfund balances and transactions, and various other disclosures.

**NOTE B: CASH AND CASH EQUIVALENTS**

In accordance with Michigan Compiled Laws, the City is authorized to invest in the following investment vehicles:

1. Bonds, securities, and other obligations of the United States or an agency or instrumentality of the United States.
2. Certificates of deposit, savings accounts, deposit accounts, or depository receipts of a State or nationally chartered bank or a State or Federally chartered savings and loan association, savings bank, or credit union whose deposits are insured by an agency of the United States government and which maintains a principal office or branch office located in this State under the laws of the State or the United States, but only if the bank, savings and loan association, savings bank, or credit union is eligible to be a depository of surplus funds belong to the State under Section 5 or 6 of Act No. 105 of the Public Acts of 1855, as amended, being Section 21.145 and 21.146 of Michigan Compiled Laws.
3. Commercial paper rated at the time of purchase within the three (3) highest classifications established by not less than two (2) standard rating services and which matures not more than 270 days after the date of purchase.
4. The United States government or federal agency obligations repurchase agreements.
5. Bankers acceptances of United States banks.
6. Mutual funds composed of investment vehicles, which are legal for direct investment by local units of government in Michigan.

Federal Deposit Insurance Corporation (FDIC) regulations provide that deposits of governmental units are to be separately insured for the amount of \$100,000 for deposits in an insured bank for savings deposits and \$100,000 for demand deposits. Furthermore, if specific deposits are regulated by statute or bond indenture, these specific deposits are to be separately insured for the amount of \$100,000. Michigan Compiled Laws allow for collateralization of government deposits, if the assets for pledging are acceptable to the State Treasurer under Section 3 of 1855 PA 105, MCL 21.143, to secure deposits of State surplus funds, securities issued by the Federal Loan Mortgage Corporation, Federal National Mortgage Association, or Government National Mortgage Association.

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE B: CASH AND CASH EQUIVALENTS - CONTINUED**

Deposits

As of June 30, 2004, the carrying amounts and bank balances for each type of bank account are as follows:

<u>Account Type</u>	<u>Carrying Amount</u>	<u>Bank Balance</u>
PRIMARY GOVERNMENT		
Regular checking	\$ 10,408	\$ 31,723
Savings	191,577	191,577
Money market	<u>527,816</u>	<u>525,798</u>
Total Primary Government	729,801	749,098
COMPONENT UNIT		
Savings	33,366	33,366
FIDUCIARY FUND		
Regular checking	300	303
Money market	<u>66,807</u>	<u>66,807</u>
Total Fiduciary Fund	<u>67,107</u>	<u>67,110</u>
TOTAL REPORTING UNIT	<u>\$ 830,274</u>	<u>\$ 849,574</u>

Deposits of the City are at federally insured banks located in the State of Michigan with all accounts maintained in the name of the City. As of June 30, 2004, the City accounts were insured by the FDIC for \$261,900, and the amount of \$587,674 was uninsured and uncollateralized.

Investments

As of June 30, 2004, the carrying amounts and market values for each type of investment as reported in the cash and cash equivalents captions on the basic financial statements are as follows:

<u>Investment Type</u>	<u>Carrying Amount</u>	<u>Bank Balance</u>
PRIMARY GOVERNMENT		
Uncategorized pooled investment funds	<u>\$ 1,484,205</u>	<u>\$ 1,484,235</u>

Due to significantly higher cash flow at certain periods during the year, the amount the City held as cash and cash equivalents increased significantly. As a result, the amount of uninsured and uncollateralized cash and cash equivalents were substantially higher at these peak periods than at year-end.

The cash and cash equivalents and investments referred to above have been reported in the cash and cash equivalents caption on the basic financial statements, based upon criteria disclosed in Note A. The following summarizes the categorization of these amounts as of June 30, 2004:

	<u>Primary Government</u>	<u>Component Unit</u>	<u>Fiduciary Fund</u>	<u>Total</u>
Cash and cash equivalents	\$ 2,157,016	\$ 33,366	\$ 67,107	\$ 2,257,489
Cash and cash equivalents - restricted	<u>56,990</u>	<u>-</u>	<u>-</u>	<u>56,990</u>
	<u>\$ 2,214,006</u>	<u>\$ 33,366</u>	<u>\$ 67,107</u>	<u>\$ 2,314,479</u>

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE C: INTERFUND RECEIVABLES AND PAYABLES**

The following schedule details interfund receivables and payables at June 30, 2004:

Due to General fund from:	
Major Street Fund	\$ 13,542
Sewer Fund	11,391
Fiduciary Fund	46,891
Component Unit	<u>28,926</u>
	100,750
Due to Major Street Fund from:	
Local Street Fund	19,555
Nonmajor governmental funds	<u>1,289</u>
	20,844
Due to Local Street Fund from:	
General Fund	70,247
Water Fund	185
Nonmajor governmental funds	<u>5,308</u>
	75,740
Due to Sewer Fund from:	
Major Street Fund	41,409
Local Street Fund	<u>76,510</u>
	117,919
Due to Water Fund from:	
General Fund	29,364
Major Street Fund	10,178
Sewer Fund	<u>35,963</u>
	75,505
Due to Fiduciary Fund from:	
Major Street Fund	<u>333</u>
Total interfund receivable and payable	<u>\$ 391,091</u>

Amounts appearing as interfund payables and receivables arise from two types of transactions. One type of transaction is where a fund will pay for a good or service that at least a portion of the benefit belongs to another fund. The second type of transaction is where one fund provides a good or service to another fund. Balances at the end of the year are for transfers that have not cleared as of the balance sheet date.

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE D: ADVANCES RECEIVABLE AND PAYABLE**

The following schedule details advances receivable and payable between funds of the primary government at June 30, 2004.

Advance to Local Street Fund from:	
Major Street Fund	<u>\$ 91,095</u>

The advance to the Local Street Fund from the Major Street Fund was used to finance current operations.

**NOTE E: INTERFUND TRANSFERS**

Permanent reallocation of resources between funds of the reporting entity is classified as interfund transfers. For the purpose of the statement of activities, all interfund transfers between individual governmental funds, business type funds, and component units have been eliminated.

Transfers to Local Street Fund from:	
Major Street Fund	\$ 20,397
General Fund	<u>55,619</u>
	<u>\$ 76,016</u>

**NOTE F: CAPITAL ASSETS**

Capital asset activity for the year ended June 30, 2004 was as follows:

PRIMARY GOVERNMENT

	Balance <u>July 1, 2003</u>	<u>Additions</u>	<u>Deletions</u>	Balance <u>June 30, 2004</u>
<b>Governmental activities</b>				
Capital Assets Not Being Depreciated				
Construction in progress	\$ -	\$ 10,000	\$ -	\$ 10,000
Land	99,000	-	-	99,000
Capital Assets Being Depreciated				
Buildings	68,800	-	-	68,800
Furniture and equipment	38,000	-	-	38,000
Vehicles	125,500	-	-	125,500
Infrastructure	<u>-</u>	<u>148,444</u>	<u>-</u>	<u>148,444</u>
Totals at historical cost	331,300	158,444	-0-	489,744
Less accumulated depreciation for:				
Buildings	( 68,800 )	-	-	( 68,800 )
Furniture and equipment	( 25,600 )	( 2,817 )	-	( 28,417 )
Vehicles	( 87,000 )	( 5,500 )	-	( 92,500 )
Infrastructure	<u>-</u>	<u>( 6,596 )</u>	<u>-</u>	<u>( 6,596 )</u>
Total accumulated depreciation	<u>( 181,400 )</u>	<u>( 14,913 )</u>	<u>-0-</u>	<u>( 196,313 )</u>
Capital assets, net	<u>\$ 149,900</u>	<u>\$ 143,531</u>	<u>\$ -0-</u>	<u>\$ 293,431</u>

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE F: CAPITAL ASSETS - CONTINUED**

Depreciation expense was charged to activities of the following governmental activities:

General government	\$ 2,817
Public works	<u>5,500</u>
Total depreciation expense	<u>\$ 8,317</u>

	Balance July 1, 2003	Additions	Deletions	Balance June 30, 2004
<b>Business-type activities</b>				
<b>(Sewer system)</b>				
Land	\$ 50,620	\$ -	\$ -	\$ 50,620
Sewer system	2,320,124	-	-	2,320,124
Equipment	<u>6,921</u>	<u>-</u>	<u>-</u>	<u>6,921</u>
Totals at historical cost	2,377,665	-0-	-0-	2,377,665
Less accumulated depreciation for:				
Sewer system	( 1,496,876 )	( 57,902 )	-	( 1,554,778 )
Equipment	<u>( 6,506 )</u>	<u>( 415 )</u>	<u>-</u>	<u>( 6,921 )</u>
Total accumulated depreciation	<u>( 1,503,382 )</u>	<u>( 58,317 )</u>	<u>-0-</u>	<u>( 1,561,699 )</u>
Capital assets, net	<u>\$ 874,283</u>	<u>\$( 58,317 )</u>	<u>\$ -0-</u>	<u>\$ 815,966</u>
<b>(Water system)</b>				
Water system	\$ 1,748,311	\$ 175,970	\$ -	\$ 1,924,281
Equipment	<u>6,922</u>	<u>-</u>	<u>-</u>	<u>6,922</u>
Totals at historical cost	1,755,233	175,970	-0-	1,931,203
Less accumulated depreciation for:				
Water system	( 707,090 )	( 38,862 )	-	( 745,952 )
Equipment	<u>( 6,506 )</u>	<u>( 416 )</u>	<u>-</u>	<u>( 6,922 )</u>
Total accumulated depreciation	<u>( 713,596 )</u>	<u>( 39,278 )</u>	<u>-0-</u>	<u>( 752,874 )</u>
Capital assets, net	<u>\$ 1,041,637</u>	<u>\$ 136,692</u>	<u>\$ -0-</u>	<u>\$ 1,178,329</u>
<b>COMPONENT UNIT</b>				
<b>Downtown Development Authority</b>				
Land	\$ 38,000	\$ -	\$ -	\$ 38,000
Infrastructure	<u>-</u>	<u>98,223</u>	<u>-</u>	<u>98,223</u>
Total at historical cost	38,000	98,223	-0-	136,223
Less accumulated depreciation for:				
Infrastructure	<u>-</u>	<u>( 4,911 )</u>	<u>-</u>	<u>( 4,911 )</u>
Capital assets, net	<u>\$ 38,000</u>	<u>\$ 93,312</u>	<u>\$ -0-</u>	<u>\$ 131,312</u>

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE G: LONG-TERM DEBT**

The following is a summary of changes in long-term debt (including current portion) of the City for the year ended June 30, 2004:

	Balance July 1, 2003	Additions	Deletions	Balance June 30, 2004	Amounts Due Within One Year
PRIMARY GOVERNMENT					
Governmental activities					
Accumulated Sick/Vacation	\$ 1,185	\$ 861	\$ -	\$ 2,046	\$ 511
Business-type activities					
Enterprise Funds					
Water Fund					
1981 Water Revenue Bonds	850,000	-	35,000	815,000	35,000
Accumulated Sick/Vacation	<u>6,473</u>	<u>-</u>	<u>875</u>	<u>5,598</u>	<u>1,400</u>
	856,473	-0-	35,875	820,598	36,400
Sewer Fund					
Accumulated Sick/Vacation	<u>6,473</u>	<u>-</u>	<u>875</u>	<u>5,598</u>	<u>1,400</u>
	864,131	861	36,750	828,242	38,311
COMPONENT UNIT					
Downtown Development Authority					
Notes Payable	<u>15,978</u>	<u>-</u>	<u>15,978</u>	<u>-0-</u>	<u>-</u>
	<u>\$ 880,109</u>	<u>\$ 861</u>	<u>\$ 52,728</u>	<u>\$ 828,242</u>	<u>\$ 38,311</u>

Significant details regarding outstanding long-term debt (including current portion) are presented below:

PRIMARY GOVERNMENT

Accrued Sick/Vacation

Individual employees have vested rights upon termination of employment to receive payments for unused vacation and sick leave. The dollar amounts of these vested rights including related payroll taxes, which have been accrued in the financial statements either on the respective fund Balance Sheet or the governmental-wide financial statements, amounted to approximately \$13,242 at June 30, 2004. Of this amount, \$11,196 is recorded as a liability within the Enterprise funds, in accordance with criteria disclosed in Note A.

Revenue Bonds

\$940,000 1981 Water Revenue Bonds, due in annual installments ranging from \$25,000 to \$70,000 through April 1, 2021 with interest at 5.00 percent, payable semi-annually.

\$ 815,000

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE G: LONG-TERM DEBT - CONTINUED**

Revenue Bonds - continued

The annual requirements to pay the debt principal and interest outstanding for the bonds are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 35,000	\$ 39,750	\$ 74,750
2006	35,000	38,000	73,000
2007	35,000	36,250	71,250
2008	40,000	34,500	74,500
2009	40,000	32,500	72,500
2010-2014	230,000	130,750	360,750
2015-2019	305,000	65,750	370,750
2020-2021	<u>95,000</u>	<u>5,000</u>	<u>100,000</u>
	<u>\$ 815,000</u>	<u>\$ 382,500</u>	<u>\$ 1,197,500</u>

**NOTE H: EXCESS OF EXPENDITURES OVER APPROPRIATIONS**

Michigan Public Act 621 of 1978, Sections 18 and 19, as amended, provides that a local governmental unit not incur expenditures in excess of the amounts appropriated and adopt budgets for the General Fund and all Special Revenue Funds.

In the required supplementary information, the City's budgeted expenditures in the General Fund have been shown at the functional classification level. The approved budgets of the City have been adopted at the functional level for the General Fund. Budgeted expenditures have not been presented for the Special Revenue funds because the City did not adopt budgets for those funds.

During the year ended June 30, 2004, the City incurred expenditures in the General Fund in excess of the amounts appropriated as follows:

	<u>Amounts Appropriated</u>	<u>Amounts Expended</u>	<u>Variance</u>
General Fund			
General government			
Council, boards, and commissions	\$ 36,483	\$ 41,153	\$ 4,670
Mayor	-	12,066	12,066
City Manager	56,385	59,622	3,237
Assessor	8,500	11,589	3,089
Clerk	53,689	83,614	29,925
Board of Review	514	855	341
Treasurer	31,812	57,549	25,737
City hall and grounds	55,670	59,612	3,942
Public safety			
Police services	177,160	213,122	35,962
Building inspections	5,720	15,240	9,520
Recreation and cultural			
Parks and recreation	15,840	20,368	4,528
Other financing uses			
Transfer out	-	55,619	55,619



## NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE I: RISK MANAGEMENT**

The City is exposed to various risks of loss for liability, property, inland marine, worker's compensation, electronic data processing, and employer's liability for which the City carries commercial insurance.

The City also participates in a pool, the Michigan Municipal Workers' Compensation Fund, with other municipalities for workers' compensation losses. The pool is organized under Public Act 317 of 1969, as amended. The City has no liability for additional assessments based on the claims filed against the pool nor do they have any rights to dividends.

**NOTE J: RETIREMENT PLAN**Plan Description

The City participates in the Michigan Municipal Employees Retirement System, an agent multiple-employer defined benefit pension plan that covers all eligible full-time employees of the City. The system provides retirement, disability, and death benefits to plan members and their beneficiaries.

Funding Policy

The Michigan Municipal Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to the System at 1134 Municipal Way, Lansing, Michigan 48917.

The obligation to contribute to and maintain the system for these employees was established by the City Council and by negotiation with the City's collective bargaining units. The plan requires no contribution from the employees.

Annual Pension Cost

For year ended June 30, 2004, the City's annual pension cost of \$42,393 for the plan was equal to the City's required and actual contribution. The estimated annual required contribution was determined as part of an actuarial valuation at December 31, 2001, using the entry actual age cost method. Actual required contributions are based on actual reported monthly payroll. Significant actuarial assumptions used include (a) a 8.00 percent investment rate of return (b) projected salary increases of 4.5 percent per year compounded annually, attributable to inflation (c) additional salary increases ranging from 0% to 4.16% per year depending on age, seniority and merit, and (d) assumption benefits will not increase after retirement.

The actuarial value of assets was determined using techniques that smooth the effects of short term volatility over a four (4) year period. The unfunded actuarial liability is being amortized as a level percentage of payroll over a period of thirty years.

Three (3) year trend information

	Year Ended December 31,		
	<u>2001</u>	<u>2002</u>	<u>2003</u>
Actuarial value of assets	\$ 217,691	\$ 242,308	\$ 282,739
Actuarial accrued liability (AAL) (entry age)	605,824	613,443	624,005
Unfunded AAL	388,133	371,135	341,266
Funded ratio	36 %	39 %	45 %
Covered payroll	154,106	146,129	153,392
UAAL as a percentage of covered payroll	252 %	254 %	222 %

City of Montrose

NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**NOTE J: RETIREMENT PLAN - CONTINUED**

	<u>2002</u>	Year Ended June 30, <u>2003</u>	<u>2004</u>
Annual pension cost	\$ 19,442	\$ 30,244	\$ 42,393
Percentage of APC contributed	100 %	100 %	100 %
Net pension obligation	-	-	-

This trend information was obtained from the most recently issued actuarial reports.

**NOTE K: DEFERRED COMPENSATION PLAN**

The City of Montrose offers its employees a deferred compensation plan created in accordance with Section 457 of the Internal Revenue Code. The assets of the plan were held in trust as described in IRC Section 457 (g) for the exclusive benefit of the participants and their beneficiaries. The trust requirement was designed by the Internal Revenue Service to help prevent participants from losing their retirement benefits to the claims of plan Sponsor's creditors. The custodian thereof for the exclusive benefit of the participants holds the custodial account for the beneficiaries of this Section 457 plan, and the assets may not be diverted to any other use.

The Administrators are agents of the City for purposes of providing direction to the custodian of the custodial account from time to time to the investment of the funds held in the account, transfer of assets to or from the account and all other matters. In accordance with the provisions of GASB Statement 32, plan balances and activities are not reflected in the City's financial statements.

**NOTE L: BUILDING AND ZONING FINANCIAL INFORMATION**

The City elected to report the financial activities of the building and zoning department in the General Fund. The following is the required information as it relates to this department for the year ended June 30, 2004:

REVENUES	
Building permits	\$ 17,442
EXPENDITURES	
Operating supplies	11
Contracted services	<u>15,229</u>
TOTAL EXPENDITURES	<u>15,240</u>
EXCESS OF REVENUES OVER EXPENDITURES	<u>\$ 2,202</u>

**NOTE M: FUND EQUITY DEFICITS**

The following funds had a fund equity deficit at June 30, 2004:

	<u>Deficit</u>
Primary Government	
Special Revenue Funds	
Local Street Fund	<u>\$ 66,934</u>
Component Unit	
Downtown Development Authority	<u>\$ 6,775</u>

## **REQUIRED SUPPLEMENTARY INFORMATION**

## City of Montrose

## General Fund

## BUDGETARY COMPARISON SCHEDULE

Year Ended June 30, 2004

	Budgeted Amounts			Variance with Final Budget Positive (Negative)
	Original	Final	Actual	
REVENUES				
Taxes				
Property taxes	\$ 327,095	\$ 327,095	\$ 380,061	\$ 52,966
Administration fees	3,059	3,059	10,975	7,916
Fees in lieu of taxes	-	-	3,789	3,789
Penalties and interest	5,160	5,160	5,149	(11)
Total taxes	335,314	335,314	399,974	64,660
Licenses and permits				
Cable television license	11,400	11,400	11,875	475
City licenses and permits	20,876	20,876	19,288	(1,588)
Total licenses and permits	32,276	32,276	31,163	(1,113)
Intergovernmental				
State - sales tax	218,948	218,948	203,769	(15,179)
Federal - CDBG	27,343	27,343	-	(27,343)
Total intergovernmental	246,291	246,291	203,769	(42,522)
Charges for services				
Solid waste	65,577	65,577	56,553	(9,024)
Other	2,050	2,050	675	(1,375)
Total charges for services	67,627	67,627	57,228	(10,399)
Fines and forfeits				
Parking	3,820	3,820	6,377	2,557
Interest and rents				
Interest	6,422	6,422	2,585	(3,837)
Rents	36,452	36,452	42,454	6,002
Total interest and rents	42,874	42,874	45,039	2,165
Other	10,448	10,448	3,937	(6,511)
TOTAL REVENUES	738,650	738,650	747,487	8,837
EXPENDITURES				
General government				
Council, boards, and commissions	36,483	36,483	41,153	(4,670)
Mayor	-	-	12,066	(12,066)
City Manager	56,385	56,385	59,622	(3,237)
Elections	5,462	5,462	773	4,689

## City of Montrose

## General Fund

## BUDGETARY COMPARISON SCHEDULE - CONTINUED

Year Ended June 30, 2004

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
EXPENDITURES - CONTINUED				
General government - continued				
Assessor	\$ 8,500	\$ 8,500	\$ 11,589	\$ (3,089)
Clerk	53,689	53,689	83,614	(29,925)
Board of Review	514	514	855	(341)
Treasurer	31,812	31,812	57,549	(25,737)
City Hall and grounds	55,670	55,670	59,612	(3,942)
Total general government	248,515	248,515	326,833	(78,318)
Public safety				
Police services	177,160	177,160	213,122	(35,962)
Fire services	44,882	44,882	44,056	826
Building inspections	5,720	5,720	15,240	(9,520)
Total public safety	227,762	227,762	272,418	(44,656)
Public works				
Department of public works	83,996	83,996	56,644	27,352
Street lighting	20,706	20,706	20,071	635
Sanitation	67,489	67,489	50,867	16,622
Total public works	172,191	172,191	127,582	44,609
Community and economic development				
Planning and zoning	6,378	6,378	4,074	2,304
Recreation and cultural				
Senior citizens center	1,960	1,960	1,211	749
Parks and recreation	14,811	14,811	10,368	4,443
Library	7,475	7,475	6,261	1,214
Total recreation and cultural	24,246	24,246	17,840	6,406
Capital outlay	1,029	1,029	10,000	(8,971)
TOTAL EXPENDITURES	680,121	680,121	758,747	(78,626)
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	58,529	58,529	(11,260)	(69,789)

City of Montrose

General Fund

BUDGETARY COMPARISON SCHEDULE - CONTINUED

Year Ended June 30, 2004

	<u>Budgeted Amounts</u>			Variance with Final Budget Positive (Negative)
	<u>Original</u>	<u>Final</u>	<u>Actual</u>	
OTHER FINANCING USES				
Transfer out	<u>-</u>	<u>-</u>	<u>(55,619)</u>	<u>(55,619)</u>
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES AND OTHER FINANCING USES	58,529	58,529	(66,879)	(125,408)
Fund balances, beginning of year	<u>216,842</u>	<u>216,842</u>	<u>216,842</u>	<u>-0-</u>
Fund balances, end of year	<u>\$ 275,371</u>	<u>\$ 275,371</u>	<u>\$ 149,963</u>	<u>\$ (125,408)</u>

## **OTHER SUPPLEMENTARY INFORMATION**

City of Montrose  
Nonmajor Governmental Funds  
COMBINING BALANCE SHEET  
June 30, 2004

	<u>Special Revenue</u>	<u>Debt Service</u>	
	<u>Depot Fund</u>	<u>Debt Service Fund</u>	<u>Total Nonmajor Governmental Funds</u>
ASSETS			
Cash and cash equivalents	<u>\$      21,267</u>	<u>\$      6,934</u>	<u>\$      28,201</u>
LIABILITIES AND FUND BALANCES			
LIABILITIES			
Due to other funds	\$          -	\$      6,597	\$      6,597
FUND BALANCES			
Unreserved - undesignated	<u>21,267</u>	<u>337</u>	<u>21,604</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$      21,267</u>	<u>\$      6,934</u>	<u>\$      28,201</u>



City of Montrose

Nonmajor Governmental Funds

COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES

Year Ended June 30, 2004

	Special Revenue	Debt Service	Total Nonmajor Governmental Funds
	Depot Fund	Debt Service Fund	
REVENUES			
Interest	\$ 6	\$ 75	\$ 81
Other			
Donations and contributions	21,300	-	21,300
TOTAL REVENUES	21,306	75	21,381
EXPENDITURES			
Current			
Community and economic development	39	-	39
EXCESS OF REVENUES OVER EXPENDITURES	21,267	75	21,342
Fund balance, beginning of year	-	262	262
Fund balance, end of year	\$ 21,267	\$ 337	\$ 21,604

City of Montrose  
Component Unit Fund  
GOVERNMENTAL FUND BALANCE SHEET  
June 30, 2004

	<u>Special Revenue</u>
	<u>Downtown Development Authority</u>
ASSETS	
Cash	\$ 33,366
Due from other governmental units	
State	8,591
County	<u>2,589</u>
TOTAL ASSETS	<u><u>\$ 44,546</u></u>
LIABILITIES AND FUND (DEFICIT)	
LIABILITIES	
Due to primary government	\$ 28,926
Due to other governmental units	<u>22,395</u>
TOTAL LIABILITIES	51,321
FUND (DEFICIT)	
Unreserved - undesignated	<u>(6,775)</u>
TOTAL LIABILITIES AND FUND (DEFICIT)	<u><u>\$ 44,546</u></u>

City of Montrose

Component Unit Fund

RECONCILIATION OF THE GOVERNMENTAL FUND BALANCE SHEET  
TO THE STATEMENT OF NET ASSETS - DOWNTOWN DEVELOPMENT AUTHORITY

June 30, 2004

<b>Fund (deficit) - governmental fund</b>	<b>\$ (6,775)</b>
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Amounts reported for the governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources  
and therefore are not reported as assets in the governmental funds.

The cost of capital assets is	<u>131,312</u>
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<b>Net assets of governmental activities</b>	<b><u>\$ 124,537</u></b>
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City of Montrose

Component Unit Fund

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGE IN FUND BALANCE

Year Ended June 30, 2004

	Special Revenue
	Downtown Development Authority
REVENUES	
Taxes	\$ 46,846
Intergovernmental	56,156
Interest	701
Other	120
TOTAL REVENUES	103,823
EXPENDITURES	
Current	
Community and economic development	12,822
Capital outlay	98,223
Debt service	
Principal	15,978
Interest and fiscal charges	1,512
TOTAL EXPENDITURES	128,535
EXCESS OF REVENUES (UNDER) EXPENDITURES	(24,712)
Fund balance, beginning of year	17,937
Fund (deficit), end of year	\$ (6,775)

City of Montrose

Component Unit Fund

RECONCILIATION OF THE STATEMENT OF REVENUES,  
EXPENDITURES, AND CHANGES IN FUND BALANCE OF THE GOVERNMENTAL  
FUND TO THE STATEMENT OF ACTIVITIES - DOWNTOWN DEVELOPMENT AUTHORITY

Year Ended June 30, 2004

**Net change in fund balance - governmental fund** \$ (24,712)

Amounts reported for governmental activities in the statement of activities are different because:

Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts are:

Capital outlay	98,223
Depreciation expense	<u>(4,911)</u>

Excess of capital outlay over depreciation expense	93,312
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Repayment of long-term debt and borrowing of long-term debt is reported as expenditures and other financing sources in governmental funds, but the repayment reduces long-term liabilities and the borrowings increase long-term liabilities in the statement of net assets. In the current year, these amounts consist of:

Repayment of note payable	15,978
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Some items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:

Decrease in accrued interest payable	<u>378</u>
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<b>Change in net assets of governmental activities</b>	<u><u>\$ 84,956</u></u>
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Principals

Dale J. Abraham, CPA  
Michael T. Gaffney, CPA  
Steven R. Kirinovic, CPA  
Aaron M. Stevens, CPA  
Eric J. Glashouwer, CPA

Karen A. Roka, CPA  
James A. Huguelet, CPA  
Alan D. Panter, CPA  
William I. Tucker IV, CPA  
Kurt M. Lemmen, CPA



ABRAHAM & GAFFNEY, P.C.  
Certified Public Accountants

Member:  
American Institute of  
Certified  
Public Accountants  
and  
Michigan Association of  
Certified Public  
Accountants

MANAGEMENT LETTER

To the Honorable Mayor and  
Members of the City Council  
City of Montrose  
Montrose, Michigan

As you know, we have recently completed our audit of the records of the City of Montrose, Michigan as of and for the year ended June 30, 2004. In connection with the audit, we feel that certain changes in your accounting and administrative procedures would be helpful in improving management's control and the operational efficiency of the accounting and administrative functions. These suggestions are a result of our evaluation of the internal control and our discussions with management.

1. The City should escheat unclaimed property to the State of Michigan.

During our audit, it was noted that the City had outstanding checks listed on their General Fund bank reconciliation that were more than two (2) years old. The Michigan Public Act 29 of 1995 provides that the Department report and escheat unclaimed property to the State of Michigan. This issue had been noted and reported in our audit comments last year.

We suggest the City attempt to contact the payees in an effort to clear old outstanding checks. In the event that the rightful property owners cannot be located, we suggest the City review their unclaimed property and escheat funds to the State of Michigan as necessary.

2. The City should establish a capitalization threshold in order to track material assets purchased.

During the course of our audit, it was noted the City does not have a formal capitalization threshold policy in place. This policy would set forth a dollar threshold for items purchased by the City, which would be considered material, long-lived assets which should be capitalized and depreciated. To facilitate the implementation of GASB Statement No. 34, we discussed the dollar threshold with management, who determined that a "per unit" threshold of \$1,500 would be appropriate.

We suggest the City Council adopt a capital asset policy through formal resolution and such approval be documented in the minutes to the Council meeting. We also suggest that the policy include a provision for the approval of capital asset disposals in order to strengthen the internal controls related to the sale or disposition of capital assets.

3. Budgets should be amended in accordance with resolutions adopted by City Council.

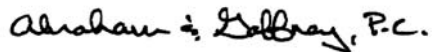
During the course of our audit, we noted that amendments affecting the total budgeted expenditures of various departments had been recorded in the City's general ledger software without the prior approval of the City Council. City Council allows management to make line item amendments without prior approval if the total departmental expenditures are not changed. Because City Council did not approve such amendments to total budgeted expenditures, the financial statements for the City do not reflect the amendments that were posted to the City's general ledger.

We suggest that management obtain Council approval when budget amendments affect total budgeted expenditures prior to recording the amendments in the general ledger, in accordance with the City Council's budget resolution.

These conditions were considered in determining the nature, timing, and extent of the audit tests to be applied in our audit of the financial statements. These conditions did not affect our report on the financial statements dated October 6, 2004.

This report is intended solely for the information of management and the Mayor and Members of the City Council of the City of Montrose and is not intended to be, and should not be, used by anyone other than these specified parties.

We wish to express our appreciation for the courtesy and cooperation extended to us during our audit. We are available to discuss any or all of these suggestions with you and to provide assistance in the implementation of improvements.



ABRAHAM & GAFFNEY, P.C.  
Certified Public Accountants

October 6, 2004